

APPENDIX C TO PART 30—OCC GUIDELINES ESTABLISHING STANDARDS FOR RESIDENTIAL MORTGAGE LENDING PRACTICES

TABLE OF CONTENTS

- I. Introduction
 - A. Scope
 - B. Preservation of Existing Authority
 - C. Relationship to Other Legal Requirements
 - D. Definitions
- II. Standards for Residential Mortgage Lending Practices
 - A. General
 - B. Objectives
- III. Implementation of Residential Mortgage Lending Standards
 - A. Avoidance of Particular Loan Terms, Conditions, and Features
 - B. Prudent Consideration of Certain Loan Terms, Conditions and Features
 - C. Enhanced Care To Avoid Abusive Loan Terms, Conditions, and Features in Certain Mortgages
 - D. Avoidance of Consumer Misunderstanding
 - E. Purchased and Brokered Loans
 - F. Monitoring and Corrective Action

I. INTRODUCTION

i. These OCC Guidelines for Residential Mortgage Lending Practices (Guidelines) set forth standards pursuant to Section 39 of the Federal Deposit Insurance Act, 12 U.S.C. 1831p-1 (Section 39). The Guidelines are designed to protect against involvement by national banks and their operating subsidiaries, either directly or through loans that they purchase or make through intermediaries, in predatory or abusive residential mortgage lending practices that are injurious to bank customers and that expose the bank to credit, legal, compliance, reputation, and other risks. The Guidelines focus on the substance of activities and practices, not the creation of policies. The Guidelines are enforceable under Section 39 in accordance with the procedures prescribed by the regulations in 12 CFR part 30.

ii. As the OCC has previously indicated in guidance to national banks and in rule-making proceedings (OCC Advisory Letters 2003-2 and 2003-3 (Feb. 21, 2003)), many of the abusive practices commonly associated with predatory mortgage lending, such as loan flipping and equity stripping, will involve conduct that likely violates the Federal Trade Commission Act's (FTC Act) prohibition against unfair or deceptive acts or practices. 15 U.S.C. 45. In addition, loans that involve violations of the FTC Act, or mortgage loans based predominantly on the foreclosure or liquidation value of the borrower's collateral without regard to the borrower's ability to repay the loan according to its

terms, will involve violations of OCC regulations governing real estate lending activities. 12 CFR 34.3 (Lending Rules).

iii. In addition, national banks and their operating subsidiaries must comply with the requirements and Guidelines affecting appraisals of residential mortgage loans and appraiser independence. 12 CFR part 34, subpart C, and the Interagency Appraisal and Evaluation Guidelines (OCC Advisory Letter 2003-9 (October 28, 2003)). For example, engaging in a practice of influencing the independent judgment of an appraiser with respect to a valuation of real estate that is to be security for a residential mortgage loan would violate applicable standards.

iv. Targeting inappropriate credit products and unfair loan terms to certain borrowers also may entail conduct that violates the FTC Act, as well as the Equal Credit Opportunity Act (ECOA) and the Fair Housing Act (FHA). 15 U.S.C. 1691 *et seq.* 42 U.S.C. 3601 *et seq.* For example, "steering" a consumer to a loan with higher costs rather than to a comparable loan offered by the bank with lower costs for which the consumer could qualify, on a prohibited basis such as the borrower's race, national origin, age, gender, or marital status, would be unlawful.

v. OCC regulations also prohibit national banks and their operating subsidiaries from providing lump sum, single premium fees for debt cancellation contracts and debt suspension agreements in connection with residential mortgage loans. 12 CFR 37.3(c)(2). Some lending practices and loan terms, including financing single premium credit insurance and the use of mandatory arbitration clauses, also may significantly impair the eligibility of a residential mortgage loan for purchase in the secondary market.

vi. Finally, OCC regulations and supervisory guidance on fiduciary activities and asset management address the need for national banks to perform due diligence and exercise appropriate control with regard to trustee activities. See 12 CFR 9.6 (a) and Comptroller's Handbook on Asset Management. For example, national banks should exercise appropriate diligence to minimize potential reputation risks when they undertake to act as trustees in mortgage securitizations.

A. *Scope.* These Guidelines apply to the residential mortgage lending activities of national banks, federal branches and agencies of foreign banks, and operating subsidiaries of such entities (except brokers, dealers, persons providing insurance, investment companies, and investment advisers).

B. *Preservation of Existing Authority.* Neither Section 39 nor these Guidelines in any way limits the authority of the OCC to address unsafe or unsound practices or conditions, unfair or deceptive practices, or other violations of law. The OCC may take action

under Section 39 and these Guidelines independently of, in conjunction with, or in addition to any other enforcement action available to the OCC.

C. Relationship to Other Legal Requirements. Actions by a bank in connection with residential mortgage lending that are inconsistent with these Guidelines or Appendix A to this Part 30 may also constitute unsafe or unsound practices for purposes of section 8 of the Federal Deposit Insurance Act, 12 U.S.C. 1818, unfair or deceptive practices for purposes of section 5 of the FTC Act, 15 U.S.C. 45, and the OCC Lending Rules, 12 CFR 34.3, or violations of the ECOA and FHA.

D. Definitions.

1. Except as modified in these Guidelines, or unless the context otherwise requires, the terms used in these Guidelines have the same meanings as set forth in sections 3 and 39 of the Federal Deposit Insurance Act, 12 U.S.C. 1813 and 1831p–1.

2. For purposes of these Guidelines, the following definitions apply:

a. Residential mortgage loan means any loan or other extension of credit made to one or more individuals for personal, family, or household purposes secured by an owner-occupied 1–4 family residential dwelling, including a cooperative unit or mobile home.

b. Bank means any national bank, federal branch or agency of a foreign bank, and any operating subsidiary thereof that is subject to these Guidelines.

II. STANDARDS FOR RESIDENTIAL MORTGAGE LENDING PRACTICES

A. General. A bank's residential mortgage lending activities should reflect standards and practices consistent with and appropriate to the size and complexity of the bank and the nature and scope of its lending activities.

B. Objectives. A bank's residential mortgage lending activities should reflect standards and practices that:

1. Enable the bank to effectively manage the credit, legal, compliance, reputation, and other risks associated with the bank's consumer residential mortgage lending activities.

2. Effectively prevent the bank from becoming engaged in abusive, predatory, unfair, or deceptive practices, directly, indirectly through mortgage brokers or other intermediaries, or through purchased loans.

III. IMPLEMENTATION OF RESIDENTIAL MORTGAGE LENDING STANDARDS

A. Avoidance of Particular Loan Terms, Conditions, and Features. A bank should not become involved, directly or indirectly in residential mortgage lending activities involving abusive, predatory, unfair or deceptive lending practices, including, but not limited to:

1. *Equity Stripping and Fee Packing.* Repeat refinancings where a borrower's equity is depleted as a result of financing excessive fees for the loan or ancillary products.

2. *Loan Flipping.* Repeat refinancings under circumstances where the relative terms of the new and refinanced loan and the cost of the new loan do not provide a tangible economic benefit to the borrower.

3. *Refinancing of Special Mortgages.* Refinancing of a special subsidized mortgage that contains terms favorable to the borrower with a loan that does not provide a tangible economic benefit to the borrower relative to the refinanced loan.

4. *Encouragement of Default.* Encouraging a borrower to breach a contract and default on an existing loan prior to and in connection with the consummation of a loan that refinances all or part of the existing loan.

B. Prudent Consideration of Certain Loan Terms, Conditions and Features. Certain loan terms, conditions and features, may, under particular circumstances, be susceptible to abusive, predatory, unfair or deceptive practices, yet may be appropriate and acceptable risk mitigation measures, consistent with safe and sound lending, and benefit customers under other circumstances. A bank should prudently consider the circumstances, including the characteristics of a targeted market and applicable consumer and safety and soundness safeguards, under which the bank will engage directly or indirectly in making residential mortgage loans with the following loan terms, conditions and features:

1. Financing single premium credit life, disability or unemployment insurance.

2. Negative amortization, involving a payment schedule in which regular periodic payments cause the principal balance to increase.

3. Balloon payments in short-term transactions.

4. Prepayment penalties that are not limited to the early years of the loan, particularly in subprime loans.

5. Interest rate increases upon default at a level not commensurate with risk mitigation.

6. Call provisions permitting the bank to accelerate payment of the loan under circumstances other than the borrower's default under the credit agreement or to mitigate the bank's exposure to loss.

7. Absence of an appropriate assessment and documentation of the consumer's ability to repay the loan in accordance with its terms, commensurate with the type of loan, as required by Appendix A of this part.

8. Mandatory arbitration clauses or agreements, particularly if the eligibility of the loan for purchase in the secondary market is thereby impaired.

9. Pricing terms that result in the loan's being subject to the provisions of the Home

Comptroller of the Currency, Treasury

§31.1

Ownership and Equity Protection Act. 15 U.S.C. 1639 *et seq.*

10. Original principal balance of the loan in excess of appraised value.

11. Payment schedules that consolidate more than two periodic payments and pay them in advance from the loan proceeds.

12. Payments to home improvement contractors under a home improvement contract from the proceeds of a residential mortgage loan other than by an instrument payable to the consumer, jointly to the consumer and the contractor, or through an independent third party escrow agent.

C. *Enhanced Care to Avoid Abusive Loan Terms, Conditions, and Features in Certain Mortgages.* A bank may face heightened risks when it solicits or offers loans to consumers who are not financially sophisticated, have language barriers, or are elderly, or have limited or poor credit histories, are substantially indebted, or have other characteristics that limit their credit choices. In connection with such consumers, a bank should exercise enhanced care if it employs the residential mortgage loan terms, conditions, and features described in paragraph B of this section III, and should also apply appropriate heightened internal controls and monitoring to any line of business that does so.

D. *Avoidance of Consumer Misunderstanding.* A bank's residential mortgage lending activities should include provision of timely, sufficient, and accurate information to a consumer concerning the terms and costs, risks, and benefits of the loan. Consumers should be provided with information sufficient to draw their attention to these key terms.

E. *Purchased and Brokered Loans.* With respect to consumer residential mortgage loans that the bank purchases, or makes through a mortgage broker or other intermediary, the bank's residential mortgage lending activities should reflect standards and practices consistent with those applied by the bank in its direct lending activities and include appropriate measures to mitigate risks, such as the following:

1. Criteria for entering into and continuing relationships with intermediaries and originators, including due diligence requirements.

2. Underwriting and appraisal requirements.

3. Standards related to total loan compensation and total compensation of intermediaries, including maximum rates, points, and other charges, and the use of overages and yield-spread premiums, structured to avoid providing an incentive to originate loans with predatory or abusive characteristics.

4. Requirements for agreements with intermediaries and originators, including with respect to risks identified in the due diligence process, compliance with appropriate bank

policies, procedures and practices and with applicable law (including remedies for failure to comply), protection of the bank against risk, and termination procedures.

5. Loan documentation procedures, management information systems, quality control reviews, and other methods through which the bank will verify compliance with agreements, bank policies, and applicable laws, and otherwise retain appropriate oversight of mortgage origination functions, including loan sourcing, underwriting, and loan closings.

6. Criteria and procedures for the bank to take appropriate corrective action, including modification of loan terms and termination of the relationship with the intermediary or originator in question.

F. *Monitoring and Corrective Action.* A bank's consumer residential mortgage lending activities should include appropriate monitoring of compliance with applicable law and the bank's lending standards and practices, periodic monitoring and evaluation of the nature, quantity and resolution of customer complaints, and appropriate evaluation of the effectiveness of the bank's standards and practices in accomplishing the objectives set forth in these Guidelines. The bank's activities also should include appropriate steps for taking corrective action in response to failures to comply with applicable law and the bank's lending standards, and for making adjustments to the bank's activities as may be appropriate to enhance their effectiveness or to reflect changes in business practices, market conditions, or the bank's lines of business, residential mortgage loan programs, or customer base.

[70 FR 6332, Feb. 7, 2005]

PART 31—EXTENSIONS OF CREDIT TO INSIDERS AND TRANSACTIONS WITH AFFILIATES

Sec.

31.1 Authority.

31.2 Insider lending restrictions and reporting requirements.

APPENDIX A TO PART 31—INTERPRETATIONS

APPENDIX B TO PART 31—COMPARISON OF SELECTED PROVISIONS OF PART 31 AND PART 32 (AS OF OCTOBER 1, 1996)

AUTHORITY: 12 U.S.C. 93a, 375a(4), 375b(3), 1817(k), and 1972(2)(G).

SOURCE: 61 FR 54536, Oct. 21, 1996, unless otherwise noted.

§31.1 Authority.

This part is issued by the Comptroller of the Currency pursuant to 12 U.S.C. 93a, 375a(4), 375b(3), 1817(k), and 1972(2)(G), as amended.